California Housing Finance Agency
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Homeownership Program Bulletin

February 14, 2011 **Program Bulletin #2011- 07**

To: CalHFA Approved Servicers

CalHFA Loan Modification Program - Update Using Keep Your Home California

This bulletin announces the implementation of the Keep Your Home California program.

The U.S. Treasury's Hardest Hit fund has allocated almost $2 billion dollars to California, one of the states hardest hit by the nation's foreclosure crisis. The Keep Your Home California (KYHC) program, administered by the California Housing Finance Agency Mortgage Assistance Corporation (CalHFA MAC), will use this funding through a number of programs that provide direct financial contributions to help reduce and prevent foreclosures statewide.

Servicers of CalHFA loans must attempt the use of KYHC in combination with the CalHFA Loan Modification Program (CMP) for homeowners with CalHFA conventional first loans. This directive is effective for loan modifications approved on or after March 15, 2011.

The Mortgage Reinstatement Assistance Program (MRAP) and Principal Reduction Program (PRP) can be used with CalHFA's CMP. Details are below, in the section "Modification Steps for CMP/KYHC Combination."

Servicers of CalHFA-owned loans are required to participate in the KYHC program and must sign a servicer participation agreement with CalHFA MAC.

Servicers must contact CalHFA MAC at 916.326.8064 by February 17, 2011, and execute the KYHC servicer participation agreement by March 15, 2011. All servicers must check potential CalHFA loan modification homeowners for KYHC eligibility before a CalHFA loan modification will be finalized. Servicers must refer all homeowners requesting a loan modification to KYHC at 888.954.KEEP(5337) for eligibility evaluation, while at the same time processing a CalHFA loan modification request. The KYHC eligibility letter and the CalHFA-approved loan modification will be combined toward the end of the process when the servicer completes and returns the KYHC updated data file and requests KYHC funds.

This bulletin offers guidance for using KYHC funds with CMP. However, it should be noted that not all CalHFA loan modifications may be eligible for KYHC due to the KYHC program qualification requirements. Loan modification requests that do not qualify for KYHC funds must be processed under the CMP in accordance with Program Bulletin #2009-12. CalHFA Loan

Modification staff will evaluate each loan modification request and incorporate the best solutions available to CalHFA homeowners requesting a loan modification.

The Combination of CMP and KYHC Consists of:

Property and Homeowner Eligibility

- The homeowner must have applied for KYHC funds.
- The mortgage must be a CalHFA first lien conventional loan originated before January 1, 2009.
- The mortgage loan must be at least two payments past due. The program may include loans in foreclosure or in the process of some other form of loss mitigation activity.
- The mortgage loan must be secured by the homeowner's principal residence.
- The homeowner must have a documented financial hardship.
- The documentation to support income must not be more than 90 days old as of the date the loan modification request is submitted to the servicer.
- Homeowners cannot currently be in bankruptcy.

Financial Hardship

A financial hardship must be fully explained and documented. Examples of financial hardships include, but are not limited to:

- Involuntary loss of employment with homeowner(s) currently unemployed.
- Temporary unemployment that has caused a significant delinquency or new employment that has resulted in less monthly income.
- Reduction in homeowner's pay (overtime eliminated, regular hours or base pay reduced) by the employer.
- One of the homeowner's incomes has been eliminated due to death, incarceration, divorce or separation.
- One of the homeowner's or wage earner's incomes has been eliminated or reduced as a result of suffering a permanent or short-term disability or serious illness.
- Self-employed homeowner has suffered a documented decline in business earnings.

Loan Counseling Requirement

The KYHC program includes eligibility determination and counseling by KYHC counselors upon a homeowner applying for KYHC program funds. If the servicer determines that formal loan counseling is advisable before a loan modification request can progress, the homeowner must attend loan counseling with a HUD-approved counseling agency. See the HUD web site at http://www.hud.gov/offices/hsg/sfh/hcc/hcs.cfm to find a local counseling agency. CalHFA may direct servicers to refer homeowners to specific counseling agencies who are knowledgeable in CalHFA programs.

Verification of Income

The servicer is required to verify the homeowner's income in accordance with the information shown on the "Loan Modification Review Checklist" (attached). For example, income may be verified using the two most recent pay stubs with year-to-date earnings, verification of supplemental income, most recent two years of tax returns and related schedules, and verbal verification of continued employment. CalHFA determines loan modification eligibility of homeowners based on a combination of net income cash flow, and a gross income Housing Debt-to-Income ratio (DTI) of principal, interest, taxes, insurance, and impounded homeowner's association dues (PITIA) to determine affordability and sustainability.

It should be noted that in the KYHC MRAP and PRP programs, homeowners with an existing Housing DTI of less than 31% are not eligible. KYHC program criteria are also subject to change; servicers may obtain current program information from the KYHC web site, www.KeepYourHomeCalifornia.org.

Verification of KYHC Assistance

KYHC will determine the type and amount of assistance the homeowner is eligible to receive and communicate the terms to the servicer. The servicer must complete the "Loan Modification Review Checklist" (attached) advising CalHFA whether KYHC has determined the homeowner is eligible for MRAP or PRP, is not eligible for KYHC funds, or does not wish to apply for KYHC assistance. This determination is required before CalHFA can proceed with evaluating the loan modification request.

Modification Steps for CMP and KYHC Combination

Step 1: Delinquent Arrearages. If a homeowner has been approved by KYHC, for the Mortgage Reinstatement Assistance Program, those funds will be applied as the first step of the loan modification up to $15,000 of past due PITIA. Servicer-paid advances on behalf of the homeowner may also be included in MRAP funds once all past due PITIA is applied.

Loans must be brought current to receive MRAP funds and, therefore, past due payments exceeding those approved by KYHC may be either paid by the homeowner, or capitalized into the CalHFA loan unpaid principal balance.

Late fees and penalties are not included in the MRAP or CMP calculations and must be waived by the servicer at the time of loan modification.

If a homeowner is eligible for the Principal Reduction Program (see Step 2 below) any past due amounts may be combined with the PRP. If KYHC funds are not approved, the total past due payments may be capitalized into the CalHFA loan unpaid principal balance for evaluation under the existing CMP as described in Program Bulletin #2009-12 CalHFA Loan Modification Program.

Step 2: Principal Reduction. If a homeowner has been approved by KYHC for the Principal Reduction Program PRP funds may be used to reduce the loan balance, and if applicable, include past due PITIA. Servicer-paid advances on behalf of the homeowner may also be included in PRP funds, provided all past due amounts and allowable advanced amounts are capitalized into the unpaid principal loan balance.

The servicer is required to waive all late fees and penalties at the time of loan modification. The PRP amount will then be used to pay down the unpaid principal balance including any capitalized amounts.

The maximum amount per household of all KYHC assistance including PRP is $50,000. Other KYHC programs are described in CalHFA Program Bulletin #2011-06 Keep Your Home California Summary. The maximum PRP amount is the lesser of $50,000 or that which will pay the loan balance down to less than 115% loan-to-value ratio of current value.

If the PRP amount is sufficient to reach an affordable housing payment, as determined by KYHC and based solely on KYHC funds, CalHFA will issue a loan modification approval based solely on KYHC assistance. If, in addition to the KYHC funds, further assistance is required, CalHFA will proceed with the evaluation under Step 3: Loan Term and Interest Rate.

If KYHC PRP funds are not approved, CMP will not reduce principal and the loan modification request will be evaluated by using the loan modification methods described in Program Bulletin #2009-12, CalHFA Loan Modification Program.

Step 3: Loan Term and Interest Rate. If, after the MRAP and/or PRP funds are approved by KYHC and further assistance is necessary to produce a sustainable loan modification, CalHFA will first apply a loan term extension up to 480 months.

Second, if necessary, CalHFA will apply a combination of loan term extension up to 480 months and a temporary interest rate reduction (no lower than 3%) to reduce the monthly mortgage payment amount according to the schedule below to achieve a Housing DTI of equal to or less than 45% (PITIA divided by gross income) with monthly residual income surplus between breakeven and $500 (the difference between net income and all monthly expenses). Loan modifications involving loan term extension and interest rate reductions must also be approved by the financial guarantor and, where applicable, a mortgage insurer.

Loan term and interest rate reduction limits are as follows:

- **For 30 and 40-year fixed rate amortizing loans**, the calculation is based on the first modified payment amount that achieves a Housing DTI of equal to or less than 45%.
- Extension of the term of the mortgage loan cannot exceed 480 months.
- The beginning temporarily reduced interest rate that achieves a Housing DTI of equal to or less than 45% cannot be less than 3.00% from the effective date of the modification.
- Note rates will be reduced in increments of one-eighth percent (0.125%). The reduced rate will be in effect for the first three years. The interest rate will incrementally increase to the original Note rate beginning in the 61st month.
  - Months 1 – 36: The payment is based on the initial reduced interest rate and/or adjusted term.
  - Months 37 – 48: The payment step up is based on the initial reduced interest rate plus step up interest rate proration. The step up rate is determined by calculating the difference between the original interest rate minus initial modification rate divided by 3, rounded up to nearest 1/8 percent.
  - Months 49 – 60: The second step up payment is based on the initial reduced interest rate plus the first and second step up interest rate pro-rations.
  - Months 61+: The payment is based on original interest rate.

The chart below is an example of an interest rate step up for a 30 or 40-year Fixed Rate with a note rate of 6%, and the minimum reduced interest rate starts at 3%, which shows the incremental increases in interest rate over five years to ultimately increase to the original note rate in the 61st month. Note rates step up in equal increases from reduced rate to original rate.

Example of 30 and 40-Year Fixed Rate Loan Step Up	
Months 1-36	3.00%
Months 37-48	4.00%
Months 49-60	5.00%
Months 61+	6.00%

- **For *interest only* PLUS℠ loans** that are still within the interest-only payment period, the Housing DTI of equal to or less than 45% is calculated on the modified fully amortized payment on the 37th month of the modification period.
- Extension of the term of the mortgage loan cannot exceed 456 months for *interest only* PLUS loans.
- The beginning temporary reduced interest rate cannot be less than 3.00% from the effective date of the modification.
- Note rates will be reduced in increments of one-eighth percent (0.125%) in order to achieve the targeted Housing DTI. The reduced rate will be in effect for the first four years for interest only PLUS loans (interest-only payments for the first three (3) years and a fully amortizing payment in the fourth year). The interest rate will incrementally increase to the original Note rate beginning in the 73rd month.
  - Months 1 – 36: Interest-only payment based on the initial reduced interest rate and/or adjusted term. Loans with a remaining interest only period of more than 3 years will receive a new 3-year interest only term that replaces the original.
  - Months 37 – 48: Amortizing payment based on the initial interest rate and term. Loan payments during this step-up period will be amortized over a new 35-year period.
  - Months 49 – 60: Amortizing payment based on the initial reduced interest rate plus step up interest rate proration. The step up rate is determined by calculating the difference between the original interest rate minus initial modification rate divided by 3, rounded up to nearest 1/8 percent.
  - Months 61 – 72: Amortizing payment is based on the initial reduced interest rate plus the first and second step up interest rate pro-rations.
  - Months 73+: Amortizing payment is based on original interest rate.

The chart below is an example of an interest rate step up for an *interest only PLUS* loan with a note rate of 6% and the minimum reduced interest rate starts at 3% which shows the incremental increases in interest rate over six years to ultimately increase to the original note rate, after the reduced interest rate period, in the 73rd month. Note rates step up in equal increases from reduced rate to original rate.

Example of interest only PLUS℠ Loans Interest Rate Step Up	
Months 1-36	3.00% Interest Only
Months 37-48	3.00% Fully Amortizing
Months 49-60	4.00% Fully Amortizing
Months 61-72	5.00% Fully Amortizing
Months 73+	6.00% Fully Amortizing

In the event an *interest only* PLUS loan has already converted to a fully amortized 30-Year Fixed Rate loan (the principal and interest payment period), the modification will be processed as per the fixed rate calculations shown above.

<u>KYHC Process</u>

At the same time the servicer is processing a CMP request, the servicer must also assist the homeowner in applying for the KYHC programs. Generally, the homeowner, either directly or through the servicer, contacts KYHC to start the process or is referred by a participating loan counseling agency. Only servicers who are approved by CalHFA MAC can refer borrowers to KYHC. KYHC will determine eligibility, provide program counseling, and process the KYHC application which, if approved, will ultimately become part of the CMP. KYHC will request documentation from both the homeowner and the servicer during this process. Once KYHC has evaluated the request and makes a determination, the servicer is to complete KYHC funding request and CMP's documents. KYHC will provide program term sheets and processes to the servicer.

The servicer should be aware that not all loan modification requests will meet the KYHC program requirements, but may still be eligible under CMP. Therefore, if KYHC funding is denied, the servicer shall process loan modifications to CalHFA for evaluation in accordance with Program Bulletin #2009-12 CalHFA Loan Modification Program.

Review the Loan Modification Request

The servicer is required to submit a completed loan modification package by either mail or email (not fax). Documentation required is listed on the "Loan Modification Review Checklist" (attached). The servicer should evaluate and pre-qualify all homeowners pursuant to the guidelines for the CMP and KYHC prior to the submission of the completed package. The servicer is encouraged to advise homeowners to seek tax advice to determine the potential impact of a loan modification. Servicers must send completed loan modification request packages to:

By mail: California Housing Finance Agency
Attn: Portfolio Management
P.O Box 4034 Mail Stop 125A
Sacramento CA 95812-4034

By Overnight : California Housing Finance Agency
Attn: Portfolio Management
500 Capitol Mall, Suite 400 Mail Stop 125A
Sacramento CA 95814

By email: PortfolioManagement@calhfa.ca.gov

Upon receipt of a completed package, CalHFA will review the request for compliance with loan modification guidelines. CalHFA reserves the right to request additional documentation as deemed appropriate.

Mortgage Insurer Approval and MIP Changes

The CalHFA Loss Mitigation Unit will obtain approval of loan modification requests from the mortgage insurer. If applicable, a revised mortgage insurance certification will be issued to reflect the new amount and premium.

Executing the CMP Agreement

- Upon modification approval, CalHFA Portfolio Management staff will forward (via email) to the servicer a Loan Modification Approval Letter containing execution instructions, and a corresponding CMP Loan Modification Agreement template.
- The servicer is to draw the CMP Agreement per the terms of the Modification Approval Letter on the CMP Loan Modification Agreement template (provided in MS Word format) and forward (via email) a PDF version back to CalHFA Portfolio Management for CalHFA signature.
- CalHFA Portfolio Management will forward, via Fed Ex, the CalHFA-signed CMP Loan Modification Agreement to the servicer for homeowner execution. If recordation is

required as detailed in “Recording the CMP Loan Modification Agreement” section below, both CalHFA’s and the homeowners’ signatures will have to be notarized.

- Servicer will send the CMP Loan Modification Agreement to the homeowner for signature. Within 14 calendar days of the loan modification approval date the homeowner will be required to sign and return to the servicer the CMP Loan Modification Agreement along with the first payment at the modified payment amount in the form of a cashier's check. Any alterations to the CMP Loan Modification Agreement will invalidate the document.
- In addition to the CMP Loan Modification Agreement, the homeowner will be required by KYHC to execute a KYHC non-interest bearing subordinate lien and deed of trust for the MRAP and/or PRP amount, as applicable. The KYHC subordinate promissory note and deed of trust will be prepared by the KYHC and sent directly to the homeowner. KYHC will be responsible for recording the KYHC deed of trust. Inquiries on the process of this lien need to be directed to KYHC.
- The servicer must review the modification file to ensure compliance with the CMP guidelines and record the returned CMP Loan Modification Agreement, if applicable under the circumstances detailed below in the “Recording the CMP Agreement" section.
- After the CMP Loan Modification Agreement is executed (and recorded, if applicable), the servicer will send to CalHFA:
  - The original signed CMP Loan Modification Agreement.
  - Copy of the KYHC eligibility document.
  - A servicer signed Current Status Letter (template provided by CalHFA) stating that the loan is now current as of the commencement date of the modification.
  - An IRS Form 4506T signed by the homeowner.
- Additionally, the servicer will request KYHC funds from KYHC for the loan modification in accordance with KYHC procedures and remit these to CalHFA as a principal pay down or reinstatement of past due amounts, as applicable.
- The form of the CMP Loan Modification Agreement may not be modified unless a servicer obtains CalHFA’s prior written consent.

Recording the CalHFA Loan Modification Agreement and Other Liens

For all mortgage loans that are modified pursuant to the CMP, the servicer must take the necessary steps to ensure that the modified mortgage loan retains its first lien position and is fully enforceable, including a review of a current title report. The servicer must take the necessary steps to ensure that any subordinate loans are in a junior position to the modified CalHFA first including a review of a current title report. Where a junior lien is held by a private or commercial lending (non-government) entity, the CalHFA Loan Modification Agreement must also be recorded, a subordination agreement obtained and a title endorsement issued to the original lender title insurance policy. These requirements do not apply where junior liens are held by a state or local government agency. Where a junior lien is held by a government agency, the servicer must send written notification to the government agency informing them of the CMP.

Servicing Modified Loans and KYHC Installment Funds

KYHC will remit MRAP funds to the servicer for arrearages in one installment at the commencement of the loan modification. KYHC will remit PRP funds to the servicer for principal reduction including any capitalized amounts in three equal annual installments. These installments will be paid on the 1st month of the loan modification and the anniversary dates on the 13th month and the 25th month from the commencement of the loan modification. Principal reduction installments are earned by the homeowner and will continue, provided that the homeowner maintains occupancy of the property as their primary residence and the loan remains in good standing, which is defined as:

- The loan is not delinquent by the equivalent of (3) three full monthly payments at the end of the month in which the last of the three delinquent payments was due, and

- The loan is current on the principal reduction anniversary dates of the modification, or the date the KYHC performs their funding review, whichever is later.

The servicer is required to monitor loans through normal servicing loss mitigation steps to resolve delinquencies where possible prior to the scheduled KYHC installments. To mitigate delayed homeowner payment problems from KYHC, the servicer will be given a 30 day period by KYHC to work with the homeowner on each anniversary date to make every effort to bring loans current. Once lost, good standing cannot be restored even if the homeowner subsequently cures the default.

Because the servicer will receive only one third of the total amount of the PRP in each of three scheduled installments from KYHC, the servicer is required to maintain the actual loan balance due to the investor on their servicing and investor reporting systems, which amount will be reduced after receipt of each PRP payment. However, the modified loan monthly payment is calculated and paid by the homeowner based on the modified loan balance. This assumes the total amount of PRP has been received and applied to the loan. However, CalHFA will not have received the entire amount until the third installment from the commencement of the loan modification.

The chart below shows an example of a $200,000 loan with a $30,000 KYHC principal reduction over three installments showing the incremental loan balance reduction to CalHFA:

PRP Payment Schedule	*Borrower's Monthly Payment is Based on Modified Loan Amount*	*Amount of KYHC PRP Installments assuming a $30,000 Total*	*Effect of a three installment $30,000 principal reduction on a CalHFA loan*
Initial Loan Balance	$200,000		$200,000
KYHC 1st Scheduled Installment	$170,000	$10,000	$190,000
KYHC 2nd Scheduled Installment	$170,000	$10,000	$180,000
KYHC 3rd Scheduled Installment	$170,000	$10,000	$170,000

Once the homeowner has satisfactorily fulfilled the terms of the KYHC requirements, maintained occupancy as primary residence and kept the loan in good standing for three years, the CalHFA MAC non-interest bearing subordinate loan will be forgiven and reconvened. The reduced loan balance will be permanent and the CalHFA loan modification will proceed as scheduled.

If the homeowner becomes ineligible for the KHYC program (default, move, etc.) before any of the subsequent PRP installments, no further PRP installments will be received from the KYHC program. In such cases, the actual balance due to CalHFA at the time of the last installment will prevail, and the loan modification will be reevaluated by CalHFA.

Escrow Accounts

Servicers must verify that all real estate taxes and assessments are current.

Servicers are encouraged to perform an escrow analysis prior to the commencement date of the modified loan. In the event the analysis identifies a shortage, the servicer must take steps to eliminate the shortage including collecting funds from the homeowner, advancing funds and capitalizing third party advances. Any actions taken by the servicer to eliminate the escrow shortage must be in compliance with applicable laws.

Incentive Fees

CalHFA will pay an incentive fee of $500 to the servicer after the homeowner and CalHFA execute the CMP Agreement and the initial modified payment has been received.

Reporting Requirements

Servicers will continue to follow the reporting requirements as outlined in CalHFA's Servicer's Guide, Accounting Section 4 and Monthly Delinquency Reporting, with additions to three related areas:

1. "Remittance to CalHFA" (Section 4, Page 14):
   Servicer shall report all KYHC PRP remittances to CalHFA within five (5) working days of receipt by providing a report to CalHFA Accounting showing the follow data fields (example below). Multiple payments must be itemized by individual loan number:

CalHFA Investor Loan Number	PRP Remittance Amount	Date Servicer received KYHC PRP funds
123AB0001	$5,000.00	9/30/10
789YZ0002	$7,500.00	11/14/10

2. "Reporting Requirements" (Section 4, Page 19):
   Servicer shall provide CalHFA Accounting with a month's end hard copy report summarizing all monthly KYHC PRP remittances. This report shall follow the current month end "Monthly Investor Reconciliation Trial Balance" report layout which categorizes all individual loans by bond series.
3. Servicers will need to report on the existing "Monthly Delinquency Reports" excel spreadsheet to CalHFA Portfolio Management four additional data fields that itemize the funding amounts received by the servicer for the UMA, MRAP, PRP and/or TAP programs as defined in CalHFA Program Bulletin #2011-06 Keep you Home California Summary.

Thank you for your continued support of CalHFA loan programs. With your assistance, many low and moderate income families who are facing foreclosure may retain their homes.

For questions about this program bulletin, contact the CalHFA Loss Mitigation Department by phone at 916.376.2920, or by email at PortfolioManagement@calhfa.ca.gov.

Attachment: Loan Modification Review Check List

Loan Modification Review Checklist

CalHFA Conventional Loan Modification Request Stacking Order

Check Box	Prepare Loan Modification Package in this Stacking Order on the right side of a legal sized folder	
	___ KYHC MRAP $_______________ ___ KYHC PRP $_______________ KYHC stated current appraised value $ _________	____ KYHC ineligible (per KYHC) ____ Borrower will not contact KYHC
	Schedule showing itemized delinquent amounts and costs (delinquent interest, escrow advances, etc…) to be capitalized and added to the unpaid principal balance. These projections should be no shorter than 90 days from submission to allow for review and processing.	
	Twelve (12) month payment history (from loan Servicer)	
	Hardship Letter explaining the reason for the delinquency with supporting documentation to verify hardship. Documentation supporting hardship must not be more than 90 days old as of the date the information is submitted to the servicer.	
	Homeowner(s) to provide a list of all personal expenditures (e.g. credit cards, loans, groceries, utilities, child care, insurance, gasoline, etc.)	
	Credit report (for all homeowners)	
	Verification of income (the last two (2) months' computer-generated pay stubs with YTD income)	
	Verification of all supplemental income, if applicable	
	Most recent two (2) years' federal tax returns including all schedules and K-1s, if applicable. If a homeowner is self-employed, provide two (2) years' business tax returns and YTD Profit and Loss Statement and Balance Sheet.	
	Verification of deposit (the last two (2) months' bank statements)	
	Verification of owner occupancy	
Below are items NOT needed at submission but will be needed prior to Loan Modification closing		
	Verbal verification of employment. (to be completed no more than five (5) days prior to date of the modification agreement and first payment sent to CalHFA)	
	Signed IRS Form 4506-T (Request for Transcript of Tax Return)	
	Current preliminary title report (lot book is acceptable)	

Loan modifications will be reviewed for final approval upon receipt of a completed package, which contains all the required documents. Delivery of incomplete and/or fraudulent information may result in program ineligibility.